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COLUMBIA, SOUTH CAROLINA

October 9, 2009

**VIA ELECTRONIC FILING**

The Honorable Charles Terreni  
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Public Service Commission of South Carolina  
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**Re: State Universal Service Support of Basic Local Service included in a  
Bundled Service Offering or Contract Offering  
Docket No. 2009-326-C**

Dear Mr. Terreni:

Enclosed for filing is the Direct Testimony of Joseph Gillan on behalf of the South Carolina Cable Television Association, CompSouth, NuVox Communications, and tw telecom. By copy of this letter, we are serving all parties of record with a copy of the same.

Yours truly,

ROBINSON, MCFADDEN & MOORE, P.C.

Frank R. Ellerbe, III

FRE/lla  
Enclosure

cc: Other parties of record (via email & U.S. Mail)  
John J. Pringle, Jr., Esquire (via email & U.S. Mail)

**BEFORE**  
**THE PUBLIC SERVICE COMMISSION OF**  
**SOUTH CAROLINA**  
**DOCKET NO. 2009-326-C**

IN RE:

State Universal Service Support of Basic  
Local Service Included in a Bundled  
Service Offering or Contract Offering

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**DIRECT TESTIMONY**

**OF**

**JOSEPH GILLAN**

**ON BEHALF OF**

**SOUTH CAROLINA CABLE TELEVISION ASSOCIATION,  
COMPSOUTH, TW TELECOM OF SOUTH CAROLINA LLC, AND  
NUVOX COMMUNICATIONS INC.**

1   **Q.    Please state your name, business address and occupation.**

2  
3   **A.    My name is Joseph P. Gillan. My business address is Post Office Box 7498, Daytona**  
4           **Beach, Florida 32116. I am an economist with a consulting practice specializing in**  
5           **telecommunications.**

6  
7   **Q.    Please briefly outline your educational background and related experience.**

8  
9   **A.    I am a graduate of the University of Wyoming where I received B.A. and M.A. degrees in**  
10           **economics. From 1980 to 1985, I was on the staff of the Illinois Commerce Commission**  
11           **where I had responsibility for the policy analysis of issues created by the emergence of**  
12           **competition in regulated markets, in particular the telecommunications industry. While**  
13           **at the Illinois Commission, I served on the staff subcommittee for the NARUC**  
14           **Communications Committee and was appointed to the Research Advisory Council**  
15           **overseeing NARUC's research arm, the National Regulatory Research Institute.**

16  
17           **In 1985, I left the Illinois Commission to join U.S. Switch, a venture firm organized to**  
18           **develop interexchange access networks in partnership with independent local telephone**  
19           **companies. At the end of 1986, I resigned my position of Vice President-**  
20           **Marketing/Strategic Planning to begin a consulting practice. Over the past decade, I have**  
21           **provided testimony before more than 35 state commissions (including South Carolina),**  
22           **six state legislatures, the Commerce Committee of the United States Senate, and the**  
23           **Federal/State Joint Board on Separations Reform. I have also been called to provide**

1 expert testimony before federal and state civil courts by clients as diverse as the trustees  
2 of a small competitive carrier in the Southeast to Qwest Communications. In addition, I  
3 have filed expert analysis with the Finance Ministry of the Cayman Islands and before the  
4 Canadian Radio-Telecommunications Commission.

5  
6 Finally, I serve on the Advisory Council to New Mexico State University's Center for  
7 Regulation (since 1985) and am an instructor in their "Principles of Regulation" program  
8 taught twice annually in Albuquerque. I also lecture at Michigan State University's  
9 Regulatory Studies Program ("Camp NARUC") and at the School of Laws at the  
10 University of London (England) and Northwestern University's Law School. A complete  
11 listing of my qualifications is provided in Exhibit JPG-1.

12  
13 **Q. On whose behalf are you testifying?**

14  
15 **A.** I am testifying on behalf of the South Carolina Cable Television Association ("SCCTA"),  
16 Competitive Carriers of the South ("CompSouth"), tw telecom of South Carolina llc ("tw  
17 telecom"), and NuVox Communications, Inc. ("NuVox") (collectively "USF Reform  
18 Coalition"). SCCTA is a nonprofit corporation that represents cable television systems  
19 operating within South Carolina. CompSouth is an industry association representing  
20 competitive providers of communication and information services in the southeastern  
21 states, including South Carolina. NuVox and tw telecom are certificated competitive  
22 local exchange carriers operating in South Carolina.

1

2 **Q. What is the purpose of your testimony?**

3

4 A. The purpose of my testimony is to explain why the Public Service Commission of South  
5 Carolina ("Commission") should clarify its guidelines to make clear that lines sold as  
6 parts of unregulated bundles and contract offerings cannot receive support from the State  
7 Universal Service Fund ("USF").

8

9 **Q. Does the current USF allow carriers of last resort ("COLRs") to recover support**  
10 **from the USF for lines that are included in bundles or contract offerings?**

11

12 A. No. The USF has never allowed COLRs to recover for unregulated services sold at  
13 market prices. I am recommending that the guidelines be clarified and enforced, so that  
14 South Carolina consumers are no longer taxed to support bundles and contract offerings  
15 that were deregulated by the South Carolina General Assembly after the current  
16 Guidelines and Administrative Procedures were approved by this Commission.

17

18 **Q. Which South Carolina statutory provisions impact the issue in this proceeding?**

19

20 A. S.C. Code Sections 58-9-280 and 58-9-285 are the key statutory provisions. Section 58-9-  
21 280(E) provides statutory guidance to Commission regarding the state USF, while section

1 58-9-285 deregulated bundled and contract offerings. The first of these provisions was  
2 adopted in 1996 and directed that the Commission establish the state USF.

3 In continuing South Carolina's commitment to universally available basic  
4 local exchange telephone service at affordable rates and to assist with the  
5 alignment of prices and/or cost recovery with costs, and consistent with  
6 applicable federal policies, the commission shall establish a universal  
7 service fund for distribution to a carrier(s) of last resort.<sup>1</sup>  
8

9 The basic goal of universal service is to make sure that consumers have an opportunity to  
10 subscribe to an affordable basic local exchange service, even if making such a choice  
11 available requires an explicit subsidy.<sup>2</sup> It was never a goal of universal service to  
12 subsidize every local subscriber, or every single service that a subscriber would desire.  
13 Most important to this proceeding is that the USF was never intended to provide  
14 subsidies for unregulated services that companies can price at market rates.  
15

16 **Q. Does Section 58-9-280 support the inclusion of lines sold as parts of bundles or**  
17 **contract offerings in the calculation of State USF support?**  
18

19 **A.** No. Section 58-9-280(E) provides that the USF is to be used to support the availability of  
20 *basic* local exchange service at affordable rates. The definition of services that can be  
21 supported by the State USF may only be expanded after a hearing specifically addressing

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<sup>1</sup> S.C. Code Ann. § 58-9-280(E) (Supp. 2008).

<sup>2</sup> S.C. Code Ann. § 58-9-10 (9):

The term "basic local exchange telephone service" means for residential and single-line business customers, access to basic voice grade local service with touchtone, access to available emergency services and directory assistance, the capability to access interconnecting carriers, relay services, access to operator services, and one annual local directory listing (white pages or equivalent).

1 that issue pursuant to Section 58-9-280(E)(8).<sup>3</sup> No hearing has been held authorizing the  
2 inclusion of deregulated service offerings.

3  
4 **Q. Should the Commission expand the USF fund to support deregulated bundles and**  
5 **contract offerings?**

6  
7 **A.** No. It is important to remember that every dollar of subsidy provided to a telephone  
8 company must first be extracted from the pockets of South Carolina consumers. In 2005  
9 when the General Assembly deregulated bundles and contract offerings, the Commission  
10 lost jurisdiction over what rates would be charged for those services.<sup>4</sup> Including  
11 deregulated services within the South Carolina USF is *fundamentally incompatible* with  
12 S.C. Code Section 58-9-280(E) which specifically requires that a service be held to a  
13 *maximum allowable rate* in order to qualify for subsidy:

14 The size of the USF shall be determined by the commission and shall be  
15 the sum of the difference, for each carrier of last resort, between its costs  
16 of providing basic local exchange services and the maximum amount it  
17 may charge for the services.

18 \*\*\*

19 Monies in the USF shall be distributed to a carrier of last resort upon  
20 application and demonstration of the amount of the difference between its

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<sup>3</sup> S.C. Code Ann. § 58-9-280(E)(8):

After notice and an opportunity for hearing to all affected carriers and the Office of Regulatory Staff, the commission by rule may expand the set of services within the definition of universal service based on a finding that the uniform statewide demand for such additional service is such that including the service within the definition of universal service will further the public interest; provided, however, that before implementing any such finding, the commission shall provide for recovery of unrecovered costs through the USF of such additional service by the affected carrier of last resort.

<sup>4</sup> Section 58-9-285(B)(1) provides that the "Commission must not: impose any requirements related to the terms, conditions, rates or availability of any bundled offering or contract offering."

1 cost of providing basic local exchange services and the maximum amount  
2 it may charge for such services.<sup>5</sup>  
3

4 For local services sold as part of a bundle or contract offering there is no maximum rate  
5 controlled by the Commission. Carriers are permitted to price according to market  
6 conditions and those same market conditions should determine whether a service offering  
7 is profitable or not. There is simply no basis for the Commission to charge *every*  
8 consumer in South Carolina a USF tax to offset any alleged loss experienced by an ILEC  
9 because it has chosen to offer a bundle or package of services below cost. It is the  
10 responsibility of the person subscribing to the bundle or package to compensate the  
11 ILEC; it is not a public-policy obligation for every other consumer to help pay for the  
12 service if the ILEC chooses to price below cost.  
13

14 **Q. Does the inclusion of bundles and contract offerings in the state USF calculation**  
15 **help accomplish the goals of establishing the state USF?**  
16

17 **A.** No. As this Commission noted in an early USF order, “[u]niversal service refers to a  
18 nationwide telecommunications policy of ensuring access to certain basic telephone  
19 service for all Americans at affordable rates.”<sup>6</sup> The only appropriate use of the money in  
20 the fund is to keep prices for regulated basic local service lower in rural areas than prices  
21 would otherwise be without the fund. As a practical matter, this means that only regulated

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<sup>5</sup> S.C. Code Ann. § 58-9-280(E)(4) and (5).

<sup>6</sup> Order No. 98-322, p. 23-24.



1 rates would qualify for the subsidy, since only regulated rates are rates that can be said to  
2 be set at a rate lower than they otherwise would be.

3  
4 **Q. Please explain the problems with continuing subsidies for deregulated services.**

5  
6 A. There are several problems. When the Commission had regulatory authority over  
7 services, it had mechanisms in place to exercise regulatory oversight with respect to the  
8 operations and earnings of the companies. As the Commission noted in its Orders, the  
9 guidelines were to ensure that the State USF was revenue neutral for the ILECs. The  
10 regulatory oversight mechanisms are no longer in place for deregulated services.<sup>7</sup>

11  
12 **Q. What are the other problems with subsidizing deregulated services?**

13  
14 A. Because prices for bundles and contract offerings are deregulated, prices will rise to  
15 market levels (but not beyond them). Because the subsidies cannot be shown to affect  
16 price levels, there is no legitimate basis for public support. Moreover, continuing  
17 subsidies for deregulated services fundamentally undermines the development of full  
18 price competition between competing service providers. Providing subsidy to a single  
19 carrier in a market provides that carrier an undeserved competitive advantage that other  
20 consumers must pay for through the USF tax.

21 ;

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<sup>7</sup> PSC Order No. 2001-419, p. 42, ¶ 23.

1 In an era where the relevant rates were regulated by the Commission—i.e., where the  
2 rates for *the* basic local service offering purchased by most consumers were directly set  
3 by the Commission—it may have been reasonable to assume that the subsidies provided  
4 to the ILEC were important to prevent higher prices. Such a world no longer exists. Many  
5 consumers obtain local service as part of a package that includes other unregulated  
6 services such as video, wireless, and DSL. More to the point, when basic local service is  
7 part of a bundle or contract offerings it is no longer regulated. As such, the *relevant*  
8 prices faced by most consumers are no longer regulated.

9  
10 **Q. Explain the importance of a COLR's number of access lines with respect to the**  
11 **amount of USF funding the COLR is entitled to receive?**

12  
13 **A. The Commission's Guidelines and Administrative Procedures are clear that the amount**  
14 **of authorized subsidy is to be calculated on a per-line basis. The Orders provide that:**

- 15  
16 \* "The cost studies [used by the Commission] provided a cost of  
17 service per access line for each designated USF support area."<sup>8</sup>  
18  
19 \* "A carrier of last resort ("COLR") that provides USF  
20 services...will be entitled to receive the full amount of per line  
21 USF support,"<sup>9</sup> and,  
22  
23 \* The Commission-approved costs of providing universal service on  
24 a per line basis...<sup>10</sup>

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<sup>8</sup> Order No. 2001-419, p. 42, ¶ 22. Emphasis added.

<sup>9</sup> Order No. 2001-996, Guidelines, p. 5. Emphasis added.

<sup>10</sup> Guidelines, p. 8. Emphasis added.

1       Significantly, with subsidy determined on a per-line basis, then *mathematically* the  
2       subsidy paid (which is also to say, the subsidy collected from South Carolina consumers)  
3       should decrease as access lines decrease. As more and more customers choose to receive  
4       service by buying bundles or contract offerings instead of traditional regulated products,  
5       the amount of the subsidy received by COLRs should decrease. Given industry trends  
6       and the introduction of deregulated services, the Commission should be seeing the size of  
7       the South Carolina USF decline over time.

8  
9   **Q.    Has the Commission seen the total disbursements under the SC USF decline as**  
10   **deregulated bundles and contract offerings have become more popular?**

11  
12  **A.    No. The size of the fund has remained substantially unchanged.**

13  
14  **Q.    Please summarize your testimony.**

15  
16  **A.    It can sometimes be forgotten (at least by the USF's recipients) that the purpose of the SC**  
17   **USF was not to provide guaranteed revenues to telephone companies, but to ensure that**  
18   **an affordable option for basic service be available to consumers in high cost rural areas.**  
19   **At one time, achieving this goal may have justified broadly supporting all lines, but that**  
20   **was in a much different environment. The current market has moved beyond the point**  
21   **where customers subscribe to a single basic service, to an environment where many**  
22   **customers have voluntarily moved up to a much more complex and expensive bundled**

1 packages of DSL, long distance, wireless and/or video. Customers selecting such bundles  
2 do not need a public subsidy to remain connected to the public voice network. A policy  
3 that attempts to subsidize all lines in order to protect the pricing of a service selected by a  
4 fraction of the population is inherently inefficient. The Commission must look not only to  
5 the desires of the *companies* that receive support, but to the needs and rights of the  
6 *consumers* that contribute. USF is a tax, plain and simple. As such, the Commission  
7 must make sure that its USF tax is as small and as efficient as possible.  
8

9 **Q. What are your recommendations?**  
10

11 **A.** We recommend that the Commission clarify that the public USF subsidy is limited to  
12 stand-alone basic local service offered at regulated rates, not to deregulated services sold  
13 as parts of bundles or contract service offerings and that the Guidelines and  
14 Administrative Procedures be updated to clarify that when COLRs report their eligible  
15 lines they should exclude unregulated lines including lines that are part of bundles and  
16 contract offerings.  
17

18 **Q. Does this conclude your direct testimony?**  
19

20 **A.** Yes.

**BEFORE  
THE PUBLIC SERVICE COMMISSION  
OF SOUTH CAROLINA**

**DOCKET NO. 2009-326-C**

IN RE:

State Universal Service Support of Basic  
Local Service Included in a Bundled  
Service Offering or Contract Offering

**CERTIFICATE OF SERVICE**

This is to certify that I, Leslie Allen, a legal assistant with the law firm of Robinson, McFadden & Moore, P.C., have this day caused to be served upon the person(s) named below the **DIRECT TESTIMONY OF JOSEPH GILLAN ON BEHALF OF THE SOUTH CAROLINA CABLE TELEVISION ASSOCIATION, COMPSOUTH, tw telecom of south carolina, llc, AND NUVOX COMMUNICATIONS INCORPORATED** in the foregoing matter by placing a copy of same in the United States Mail, postage prepaid, in an envelope addressed as follows:

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Dated at Columbia, South Carolina this 9<sup>TH</sup> day of October, 2009.



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Leslie Allen